

**3. Explain the difference between short-run equilibrium and long-run equilibrium in monopolistic competition. [10 marks]**

Candidates **may** include the assumptions of monopolistic competition, which **may** include:

- large number of firms
- very elastic demand
- firms are small relative to the size of the market
- no or low barriers to entry or exit
- perfect knowledge in the market
- product differentiation
- firms are short-run profit maximisers.

Candidates **may** include the difference between short-run equilibrium and long-run equilibrium, which **may** include:

- distinction between short run and long run
- definition of equilibrium
- explanation of profit maximization
- firms can make abnormal profits (economic profits) in the short-run
- abnormal profits (economic profits) will attract new entrants into the market
- demand for existing firms falls
- the process continues until normal profits (zero economic profits) are made in the long-run.

Diagrams for short-run profit and for long-run normal profit are expected. If candidates approach the question from the perspective of short-run losses, they can be fully rewarded.

Examiners should be aware that candidates might take a different approach, which should be fully rewarded if appropriate.

**4. In the theory of the firm, a distinction is made between short-run cost curves and long-run cost curves. Using appropriate cost curve diagrams, explain this distinction. [10 marks]**

Answers **should** include:

- definitions of short-run and long-run
- U shaped SRAC diagram
- diagram showing LRAC as L-shaped and/or U-shaped.

*N.B. Candidates may also include the SRMC diagram. This should be rewarded but is not necessary to achieve full marks.*

Answers **may** include:

- explanation of SRAC in terms of the law of diminishing returns
- explanation of the LRAC in terms of economies/diseconomies of scale.

*A clear distinction between SRAC and LRAC must appear in the answer, for example, in terms of diminishing returns and diseconomies/economies of scale to achieve level 4.*

Examiners should be aware that candidates may take a different approach which if appropriate, should be rewarded.